NOTES.

THE REAL ISSUES IN THE QUANTITY-THEORY CONTROVERSY.

THE recent appearance of two important books on money has started anew the controversy regarding the quantity-theory of money. The authors of both books — Professors Laughlin and Scott — devote chapters to adverse criticism of that time-honored doctrine. These criticisms have been in their turn criticised by the adherents of the views assailed, and, short though the time has been, Professor Laughlin and Professor Willis have published replies.[1] It seems not improbable that the controversy thus begun will run the familiar course through rejoinders provocative of replies, themselves to be the subject of further disputation.

Unfortunately, such controversies are no new thing in economics: but of late years they have fallen somewhat into disfavor. After more than one heated debate the consensus of opinion has been that the differences of view arose mainly from mutual misunderstandings and disappeared when the positions of the disputants had been clearly defined. Some such futile issue may be predicted in the present case, if the controversy continues as it has begun. Both parties seem to misconceive the central positions of their opponents, and in part to be disputing opinions for which no one seriously contends. The resulting waste of energy is the more unfortunate because there are important problems in the theory of prices which the misdirected energy might help to solve. It is possible that a succinct statement of what both parties agree upon concerning the connection between quantity of money and prices may help to dispel the misunderstandings and to concentrate attention upon the real problems.

[1] See J. LAURENCE LAUGHLIN, *Principles of Money* (New York: Scribner, 1903); WILLIAM A. SCOTT, *Money and Banking* (New York: Holt, 1903); FREDERICK R. CLOW, "The Quantity Theory and its Critics," JOURNAL OF POLITICAL ECONOMY, September, 1903, pp. 594–620; LAUGHLIN, "The Quantity Theory and its Critics: A Rejoinder," *ibid.*, pp. 621–25; U. S. PARKER, "An Increase in Gold and the Price-Making Process," *ibid.*, pp. 625–29; JOSEPH F. JOHNSON, "The New Theory of Prices," *Political Science Quarterly*, October, 1903; H. PARKER WILLIS, "The Controversy over Price Theories," *Sound Currency*, March, 1904.

1. No one known to me denies that prices are affected by the quantity of money, though there are differences of opinion concerning the manner and degree of the effect and the sense in which the word "money" should be understood. Certainly neither Professor Laughlin nor Professor Scott makes such denial. The former says in the course of his chapter "A Critical Examination of the Quantity Theory":

> . . . . no one doubts that an increased supply of the standard metal would affect its value, and hence affect prices; but we shall see that the quantity of the metal is but one of the several factors affecting price.[2]

In the following chapter, entitled "The True Theory of Prices," Professor Laughlin follows up this statement by dividing the forces affecting prices into forces affecting goods on the one hand and gold on the other. Regarding the latter set of forces he says:

> For practical purposes, the value of gold, so far as the elements affecting itself are concerned, is influenced mainly by its supply and demand.[3]

Professor Scott's position seems to be similar, although it is less clearly expressed. He says, for example, that in case of a rise of prices the opponents of the quantity theory

> would search for causes of the rise . . . . in changed conditions in the demand and supply of commodities or of gold or of both.[4]

And, in expounding his own theory of prices, Professor Scott says that a change of prices may be due to any one of four causes, acting singly or in combination; viz., a rise or fall in the "value" of commodities, or a rise or fall in the "value" of the standard.[5] He does not explain in what sense he uses the word "value," or how a change in the "value" of either commodities or of gold may be produced; but explicit statements are not needed to warrant the belief that Professor Scott would admit the influence of demand and supply upon the purchasing power of gold.

The dispute, then, about the fundamental proposition that the quantity of money has an effect upon the price-level is concerned, not with the validity of the proposition, but with its interpretation. Professors Laughlin and Scott regard changes in supply and demand of gold alone. But in so doing they are at one with so loyal an adherent of the quantity theory as Professor Nicholson:

> Whilst granting, then, that for certain purposes the definition of "money"

[2] *Principles of Money*, p. 327.

[3] *Ibid.*, p. 342.

[4] *Money and Banking*, p. 61.

[5] *Ibid.*, p. 35.

in the quantity theory may be extended, as for instance in the case of inconvertible paper, I think that when it is applied to the case of the appreciation of gold, or the fall in gold prices of commodities, we ought by "money" to mean gold.[6]

An avowed quantity-theorist would doubtless prefer to speak of the supply of gold money; but Nicholson also speaks simply of gold, and all parties agree that under such conditions as Laughlin, Scott, and Nicholson have in mind non-monetary changes in the supply and demand for gold may affect prices, directly or indirectly. Critics of the new treatises, therefore, who assume that Professors Laughlin and Scott's avowed hostility to the quantity theory involves denial that quantity of money affects prices mistake the issue. The dispute concerns the manner and degree of the effect, or the question whether the quantity of gold in any form, or gold coin alone, or gold coin and other forms of money, must be considered

2. No competent writer denies that other factors besides the quantity of money affect prices. Whatever some careless phrases may have implied, the recognized exponents of the theory have made it abundantly clear that in their view prices vary concomitantly with the quantity of money only when all other things remain substantially the same.[7] Accordingly, theorists who have been impressed by the importance of other price factors do not for that reason have any just cause of offense at the quantity theory. Their arguments that other factors must affect prices, and their statistical demonstrations that during certain periods prices and the quantity of the circulating medium have diverged in their fluctuations, even if perfectly sound, are not to be accepted as refutations of the theory.[8]

Professor Laughlin, indeed, recognizes this objection to his criticism, but without appreciating its full force:

To be sure, it will be said that the quantity of money as compared with the money work regulates prices, *other things being equal;* but if the "other things" are so important that changes in the quantity of the circulation on a marked scale are not followed by corresponding changes in the price level,

[6] *Treatise on Money,* 4th ed., p. 146.

[7] *E. g.,* see the vigorous statement made by PRESIDENT WALKER in reply to a criticism of the quantity theory by one of Professor Laughlin's pupils: *Quarterly Journal of Economics,* Vol. IX (1895), pp. 372–79.

[8] In this condemnation I include an undergraduate paper of my own that has been too often quoted, "The Quantity Theory of the Value of Money," JOURNAL OF POLITICAL ECONOMY, March, 1896.

then that is equivalent to proving that the "other things" are of more influence than the quantity of money.[9]

Two opinions are held about the relative importance of the quantity of money and these "other things" as price-determinants; but even conclusive proof that Professor Laughlin's opinion on that mooted point is correct would not disturb the proposition that when these "other things" are constant, prices will be affected by changes in the quantity of money. Not only, then, are Professors Laughlin and Scott misunderstood by their critics; they also misunderstand the theory which they attack. Had they paid more heed to the limitations with which the theory is stated in the better expositions, they would have conceived their own arguments, not as refuting the theory, but as showing what are its true interpretation and its relative importance in accounting for price fluctuations.

To repeat, the present controversy arises from mutual misunderstandings. The real issue is not the proposition that prices are affected by the quantity of money. No one denies that this quantity is one of the price-determinants; no one maintains that it is the sole determinant. Accordingly, the controversy does not concern the validity of the quantity theory. This statement, that there is substantial agreement upon the central proposition of the quantity theory, of course does not imply that the recent writers are at one upon the theory of prices. Quite the contrary, it is precisely because there are real and important differences of opinion that waste of time upon a mistaken issue is so unfortunate. What the real issues are has been indicated in part already; but a brief restatement in the form of questions may help to clarify a subject suffering chiefly from confusion of ideas.

1. What is the money that affects prices through its quantity? On this question there is difference of opinion not only between avowed critics of the theory and adherents, but also between different adherents. Professor Taussig, *e. g.*, in his *Silver Situation* argues that the theory must be so interpreted as to include "the total volume of *purchasing power in terms of money*."[10] Nicholson stands, as has been noted, at the other extreme with Laughlin and Scott in maintaining that "money" must mean gold alone. Between these extremes Dr. Frederick R. Clow, another professed adherent of the quantity theory, takes up an intermediate position:

[9] *Principles of Money*, p. 327; the italics are in the original.

[10] P. 63.

> Notwithstanding the ambiguity of the word "money," we may still take it to mean any one of several things — gold coin, gold and token money, or the entire medium, because these things change their proportions *pari passu,* except as the habits of the community change.[11]

Clearly, there is here a question requiring further discussion; but the line dividing the opposite parties will not be the line that divides professed adherents of the quantity theory from professed critics.

2. How does the quantity of money exert its effect on prices? In summing up the difference between his own theory of prices and the quantity theory, Professor Laughlin says that in his view the effect of changes in the supply and demand of gold upon prices is exerted through an evaluation of gold that "goes on antecedent to the exchange operation," whereas, "according to the quantity theory, the only means of arriving at the evaluation of goods and gold is by the actual use of 'money' (however defined) as a medium of exchange offered directly for goods."[12] Whether all the professed adherents of the quantity theory would accept Professor Laughlin's statement of the manner in which they conceive the quantity of money to exert its influence on prices, I do not know; for they have usually neglected to trace the process by which a change in the supply of money affects prices with the care required by the subject. But even if Professor Laughlin's statement of the difference of opinion is acceptable to his opponents, it is clear that the difference concerns, not the validity of the proposition that prices are affected, among other things, by the quantity of money, but merely *the manner in which* this effect is exerted.

3. What are the other factors affecting prices, and how do they exert their influence? It is in dealing with this question that the critics of the quantity theory have rendered their most valuable services. Forgetful of the example set by such investigators as Tooke, Newmarch, and Jevons, the quantity-theorists show an indolent disposition to let the "other things" which their statements admit vaguely as price factors severely alone. Their critics, so far as they have exploited these "other things," have helped to restore proper emphasis and stimulate discussion of neglected factors. But the work of carrying farther these investigations should be shared by both parties. On its own showing, the quantity theory is not an adequate explanation of price fluctuations, and the task of its devotees

[11] JOURNAL OF POLITICAL ECONOMY, September, 1903, p. 619.

[12] *Op. cit.*, p. 362.

is not finished until they have supplemented it by analyzing clearly the effects of whatever "other things" they admit as price factors.

4. What is the relative importance of the various price factors? This is the most difficult of all the questions, and the one on which the present supposed difference of opinion would be most nearly maintained. Perhaps there is little hope that substantial unity of opinion could be attained even after the most thorough and amicable discussion. But the discussion would certainly be more fruitful if both parties recognized that they were talking about the relative importance of the quantity of money as a price factor — not about its existence or nonexistence as a factor.

The confusion of ideas to which attention has been called does not appear at all in the writings of some of the participants in the controversy; and it does not prevent the other participants from dealing much of the time with points of genuine interest. But it does becloud a subject that is at best exceedingly complex, tending to divert attention from the matters of importance and to concentrate it upon a matter concerning which the disputants are unwittingly agreed. The discussion would gain much in clarity if all parties could realize that their task is not to debate the proposition that prices are affected by the quantity of money, but (1) to interpret, (2) to explain, (3) to supplement, and (4) to evaluate that proposition.

WESLEY C. MITCHELL.

THE UNIVERSITY OF CALIFORNIA.

THE ECONOMIC VALUE OF THE HOME.[1]

FOR the last forty years the discussion of the so-called "woman question" has been most bewildering. In order to thread one's way through it one must develop a special method of sorting out opinions according to the social rank, education, and occupations of the persons who advance arguments, must class them by the sections of the country from which those persons come — their church proclivities, political affiliations, race traditions, and personal environment — only to decide at last that no agreement is ever likely to be reached, because there are too many uncertain factors in the problem.

Mrs. Gilman's book seems destined to mark an epoch in senti-

[1] *The Home, its Work and its Influence.* By CHARLOTTE PERKINS GILMAN. New York: McClure & Philipps, 1903.